# INDEX


| | Page |
|---|---|
| Opinions below | 1 |
| Jurisdiction | 1 |
| Question presented | 2 |
| Statute involved | 2 |
| Statement | 2 |
| Argument | 6 |
| Conclusion | 10 |


## CITATIONS


Cases:

| | |
|---|---|
| *Busch* v. *Commissioner*, 148 F. 2d 798 | 6 |
| *Chertoff* v. *Commissioner*, 160 F. 2d 691 | 9 |
| *Choate* v. *Commissioner*, 324 U. S. 1 | 9 |
| *Commissioner* v. *Estate of Holmes*, 326 U. S. 480 | 8 |
| *Commissioner* v. *Tower*, 327 U. S. 280 | 9 |
| *Corliss* v. *Bowers*, 281 U. S. 376 | 6 |
| *Cutting* v. *Cutting*, 86 N. Y. 522 | 7 |
| *Dobson* v. *Commissioner*, 320 U. S. 489, rehearing denied, 321 U. S. 231 | 9 |
| *Emery* v. *Commissioner*, 156 F. 2d 728, certiorari denied, November 12, 1946, No. 555, this Term | 6 |
| *Harrison* v. *Schaffner*, 312 U. S. 579 | 6 |
| *Helvering* v. *Clifford*, 309 U. S. 331 | 6 |
| *Helvering* v. *Horst*, 311 U. S. 112 | 6 |
| *Helvering* v. *Stuart*, 317 U. S. 154 | 8 |
| *Jergens* v. *Commissioner*, 136 F. 2d 497, certiorari denied, 320 U. S. 784 | 7 |
| *Kelley, John, Co.* v. *Commissioner*, 326 U. S. 521 | 9 |
| *Mallinckrodt* v. *Nunan*, 146 F. 2d 1, certiorari denied, 324 U. S. 871 | 7 |
| *Manion* v. *Peoples Bank of Johnstown*, 292 N. Y. 317 | 8 |
| *Richardson* v. *Commissioner*, 121 F. 2d 1, certiorari denied, 314 U. S. 684 | 7 |
| *Stix* v. *Commissioner*, 152 F. 2d 562 | 6 |
| *Sweeney* v. *Warren*, 127 N. Y. 426 | 8 |

Statutes:

| | |
|---|---|
| Internal Revenue Code, Sec. 22 (26 U. S. C. 1940 ed., Sec. 22) | 2, 6 |
| Real Property Law of New York (McKinney's Consolidated Laws of New York Annotated, Art. 5), Secs. 133–138 | 7 |

# In the Supreme Court of the United States

OCTOBER TERM, 1946

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No. 1385

SYDNEY R. NEWMAN, PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE

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*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT*

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## BRIEF FOR THE RESPONDENT IN OPPOSITION

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### OPINIONS BELOW

The findings of fact and opinion of the Tax Court, together with the dissenting opinion (R. 26–36), are reported at 5 T. C. 603. The opinion of the Circuit Court of Appeals, together with the dissenting opinion (R. 42–48), is reported at 159 F. 2d 848.

### JURISDICTION

The judgment of the Circuit Court of Appeals was entered on February 20, 1947 (R. 49–50.) The petition for a writ of certiorari was filed on May 17, 1947. The jurisdiction of this Court

rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the taxpayer possessed the power to alter or amend for his own benefit two trusts created by his wife, thus giving him unfettered command over the trust income and making such income taxable to him under section 22 (a) of the Internal Revenue Code.

STATUTE INVOLVED

Internal Revenue Code:

> SEC. 22. GROSS INCOME.
>
> (a) *General definition.*—"Gross income" includes gains, profits, and income derived from interest, rent, dividends, securities, or personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> * * * * * *

(26 U. S. C. 1940 ed., Sec. 22.)

STATEMENT

The facts found by the Tax Court (R. 27–29) may be restated as follows:

Taxpayer is an attorney practicing in New York City. At all times mentioned he was mar-

ried to Lillian M. Newman, who resided with him. They are the parents of Janice and Robert Newman. (R. 27–28.)

On or about June 28, 1940, Lillian M. Newman created two trusts, each of which named taxpayer as sole trustee. One trust was for the benefit of their daughter Janice and the other for the benefit of their son Robert. At the time the children were minors. The terms of the trust instruments are identical. (R. 28.)

Under the trust instruments, taxpayer, as trustee, was given broad powers of management and control over the trust estates (R. 28). The following additional provisions, except for the difference in the name of the child-beneficiary, were contained in each trust (R. 28–29):

> Third. Subject to the power of the Trustee solely at his option from time to time to use all or any part of the income and principal of the trust fund to pay any taxes, assessments, costs, charges, or expenses incurred in the receipt, collection, care, administration, protection or distribution of the trust fund or income thereof, the Trustee shall hold, manage, invest and reinvest the said property with power to sell any investments, and to reinvest the proceeds thereof, and shall collect and receive the issues, interest and income thereof and pay over the net income and principal as follows:
>
> (a) To pay the income annually to Robert W. Newman, son of the Grantor, during

his lifetime. Upon the death of said Robert W. Newman all the rest, residue and remainder of said fund shall be paid over to Sydney R. Newman, husband of the Grantor. If the said Sydney R. Newman shall not then be living, the rest, residue and remainder of said fund shall be paid over to such person or persons as the said Sydney R. Newman by his last will and testament may direct and appoint; upon the death of said Sydney R. Newman without having exercised such power of appointment to pay the rest, residue and remainder of said fund to his distributees.

* * * * *

Tenth. Said Sydney R. Newman shall have the power at any time during his life, by an instrument in writing delivered to the Trustee, to revoke this agreement, in whole or in part, or to alter or amend the same or to free any of the property held in trust from the terms of this trust, and upon receipt of such instrument in writing, the Trustee shall turn over to the Grantor any funds or property held by the Trustee hereunder as required by said written notice, and the receipt of the Grantor for such property shall be a full acquittance to the Trustee.

The corpus of each trust consisted of securities worth approximately $10,000. Under the terms of the trust instruments, taxpayer could keep the trust securities in his own name or in the name of

a nominee. For convenience and in order to facilitate sale or other disposition, the securities remained in the name of Lillian M. Newman on the corporation records and were endorsed in blank by her. She received the dividends and paid them to taxpayer, who deposited them in a separate bank account he opened for each trust. No withdrawals have been made except to adjust a dividend payment and to purchase additional property for one of the trusts. Household expenses and the support and education of the child-beneficiaries have been paid by taxpayer from his own funds. (R. 28, 29.)

The Tax Court interpreted the trust instruments as giving the taxpayer no power to alter or amend so as to take the trust income to himself at any time. Accordingly, it held that the taxpayer did not have such dominion and control as to be considered the owner of the trust income and taxable under Section 22 (a) of the Internal Revenue Code. (R. 30–32.) Six judges dissented, disagreeing both with the majority's interpretation of the trust instruments and with the result reached on the basis of that interpretation (R. 32–36).

The Circuit Court of Appeals (Judge Learned Hand dissenting) reversed, holding that the trust instruments, construed in the light of New York law, gave the taxpayer the power to alter or amend the trusts for his own benefit with the re-

sult that he was empowered to appropriate the income to himself and that he was taxable under Section 22 (a) of the Internal Revenue Code (R. 43–46).

**ARGUMENT**

1. There can be no serious dispute with the ultimate conclusion of the court below, namely, that the trust income in question must be taxed to the taxpayer under Section 22 (a) of the Internal Revenue Code, *supra,* if he, unfettered by any fiduciary obligations, was empowered to control the trust income by means of his authority to alter or amend the trusts. Absent any restrictions on his ability to alter or amend, the taxpayer would have complete power to utilize the income for his own purposes, or to accumulate it for his own ultimate benefit since he was entitled to the gifts-over on the death of the named beneficiaries. The existence of such control, being tantamount to ownership of the income, would require taxability under Section 22 (a). See *Harrison* v. *Schaffner,* 312 U. S. 579; *Helvering* v. *Horst,* 311 U. S. 112; *Helvering* v. *Clifford,* 309 U. S. 331. Cf. *Corliss* v. *Bowers,* 281 U. S. 376. Nor would the income be any the less taxable to the taxpayer because he was not the grantor of the trusts and because his control was acquired rather than retained. *Emery* v. *Commissioner,* 156 F. 2d 728 (C. C. A. 1st), certiorari denied November 12, 1946, No. 555, this Term; *Stix* v. *Commissioner,* 152 F. 2d 562 (C. C. A. 2d); *Busch* v. *Commissioner,* 148 F. 2d

798 (C. C. A. 8th); *Mallinckrodt* v. *Nunan,* 146 F. 2d 1 (C. C. A. 8th), certiorari denied, 324 U. S. 871; *Jergens* v. *Commissioner,* 136 F. 2d 497 (C. C. A. 5th), certiorari denied, 320 U. S. 784; *Richardson* v. *Commissioner,* 121 F. 2d 1 (C. C. A. 2d), certiorari denied, 314 U. S. 684.

The court below was correct in concluding that the power given by the trust instruments to the taxpayer to alter or amend the trusts was one which he could exercise without any fiduciary limitations, and which he could utilize for his own purposes without regard to any resulting detriment to the interests of his children who were named as beneficiaries. Under New York law, a beneficial power is one in the execution of which no person other than the grantee has any interest, while a power in trust is one in which some person or class of persons is designated as entitled to the proceeds or other benefits resulting from its execution. See Sections 133–138 of the Real Property Law of New York (McKinney's Consolidated Laws of New York Annotated, Art. 5), and *Cutting* v. *Cutting,* 86 N. Y. 522, holding that the statutory rules regarding powers apply to personal property as well as to real property. The trust instruments here referred to the "Trustee" in enumerating the power and duties of the taxpayer acting as a fiduciary; significantly, however, the power to alter or amend was granted to the taxpayer individually, by name, without any suggestion that he was to exercise it in a fiduciary

capacity (R. 36–40). See *Commissioner* v. *Estate of Holmes,* 326 U. S. 480. This, together with the circumstance that the trust instruments did not give the children any beneficial interest in the exercise of the power to alter or amend, is strongly persuasive that the power was not in trust but was a beneficial power which the taxpayer could exercise for his own benefit. *Manion* v. *Peoples Bank of Johnstown,* 292 N. Y. 317; *Sweeney* v. *Warren,* 127 N. Y. 426. Accordingly, applying New York law in the construction of the trust instruments, the Circuit Court of Appeals was right in ruling that the taxpayer could have exercised the power for his own benefit.

2. There is no conflict in decisions. *Helvering* v. *Stuart,* 317 U. S. 154, which is alleged (Pet. 10–15, 22–23) to be opposed to the decision below is, on the contrary, persuasive authority in support of the decision of the Circuit Court of Appeals. In the *Stuart* case, it was held that the reasoned judgment of a Circuit Court of Appeals respecting the application of the law of a state which is within the jurisdiction of that circuit will not be reversed unless there has been a clear demonstration of error. Further, it was observed (p. 164) that there was no reason why the view of the Board of Tax Appeals in that case concerning Illinois law should be preferred to that of the Circuit Court of Appeals. In the present case, too, there is no reason why the application of New

York law by the Tax Court in the construction of the trust instruments here should be more compelling than that of the Circuit Court of Appeals. The *Stuart* case also demonstrates that the other cases relied on as creating conflicts in decisions regarding the scope of review to be afforded the Tax Court's conclusions (*Dobson* v. *Commissioner,* 320 U. S. 489, rehearing denied, 321 U. S. 231 (Pet. 16–18, 23); *Choate* v. *Commissioner,* 324 U. S. 1 (Pet. 18); *Commissioner* v. *Tower,* 327 U. S. 280 (Pet. 18); *John Kelley Co.* v. *Commissioner,* 326 U. S. 521 (Pet. 18–19); and *Chertoff* v. *Commissioner,* 160 F. 2d 691 (C. C. A. 6th) (Pet. 33–36)) are not at all opposed to the decision below. The disagreement between the Tax Court and the Circuit Court of Appeals in this case did not concern the application of the taxing statute; instead, it only related to the extent of the taxpayer's powers under the trust instruments in the light of New York law. The Circuit Court of Appeals, being convinced that the Tax Court had erroneously interpreted the instruments in the light of that law, was certainly empowered to reverse. Where the Tax Court's decision was premised on an error of state law which led it to a wrong conclusion respecting the taxpayer's powers over the trust income, it cannot be said that a clear-cut mistake of law is lacking or that its decision finds warrant in the record.

## CONCLUSION

The decision below is correct. There is no conflict in decisions. Accordingly, further review of this case would not be warranted, and the petition for a writ of certiorari should be denied.

Respectfully submitted.

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